

**§ 703.110 What investments and investment activities are prohibited for me?**

(a) You (a federal credit union) may not purchase or sell financial derivatives, such as futures, options, interest rate swaps, or forward rate agreements, except as permitted under § 701.21(i) of this chapter.

(b) You may not engage in adjusted trading or short sales.

(c) You may not purchase stripped mortgage backed securities, residual interests in CMOs/REMICs, mortgage servicing rights, commercial mortgage related securities, or small business related securities.

(d) You may not purchase a zero coupon investment with a maturity date that is more than 10 years from the settlement date.

**§ 703.120 May my officials or employees accept anything of value in connection with an investment transaction?**

(a) Your (a federal credit unions) officials and senior management employees, and their immediate family members, may not receive anything of value in connection with your investment transactions. This prohibition also applies to any other employee, such as an investment officer, if the employee is directly involved in investments, unless your board of directors determines that the employee's involvement does not present a conflict of interest. This prohibition does not include compensation for employees.

(b) Your officials and employees must conduct all transactions with business associates or family members that are not specifically prohibited by paragraph (a) of this section at arm's length and in your best interest.

(c) Senior management employee means your chief executive officer (typically this individual holds the title of President or Treasurer/Manager), any assistant chief executive officers (e.g., Assistant President, Vice President, or Assistant Treasurer/Manager) and the chief financial officer (Comptroller).

(d) Immediate family member means a spouse or other family member living in the same household.

**§ 703.130 May I continue to hold investments purchased before January 1, 1998, that will be impermissible after that date?**

(a) Subject to safety and soundness considerations, you may hold a CMO/REMIC residual, SMBS, or zero coupon security with a maturity greater than 10 years, if you purchased the investment:

(1) Before December 2, 1991; or

(2) On or after December 2, 1991, but before January 1, 1998, if for the purpose of reducing interest rate risk and you meet the following:

(i) You have a monitoring and reporting system in place that provides the documentation necessary to evaluate the expected and actual performance of the investment under different interest rate scenarios;

(ii) You use the monitoring and reporting system to conduct and document an analysis that shows, before purchase, that the proposed investment will reduce your interest rate risk;

(iii) After purchase, you evaluate the investment at least quarterly to determine whether or not it actually has reduced your interest rate risk; and

(iv) You classify the investment as either trading or available-for-sale.

(b) All grandfathered investments are subject to the valuation and monitoring requirements of §§ 703.70, 703.80, and 703.90.

[63 FR 24105, May 1, 1998]

**§ 703.140 What is the investment pilot program and how can I participate in it?**

(a) Under the investment pilot program, NCUA will permit a limited number of federal credit unions to engage in investment activities prohibited by this part but permitted by statute.

(b) Except as provided in paragraph (c) of this section, before you (a federal credit union) may engage in additional activities, you must obtain written approval from

NCUA. To begin the approval process, you must submit a request to your regional director that addresses the following items:

(1) Board policies approving the activities and establishing limits on them.

(2) A complete description of the activities, with specific examples of how you will conduct them and how they will benefit you.

(3) A demonstration of how the activities will affect your financial performance, risk profile, and asset-liability management strategies.

(4) Examples of reports you will generate to monitor the activities.

(5) A projection of the associated costs of the activities, including personnel, computer, audit, etc.

(6) A description of the internal systems to measure, monitor, and report the activities, and the qualifications of the staff and/or official(s) responsible for implementing and overseeing the activities.

(7) The internal control procedures you will implement, including audit requirements.

(c) You need not obtain individual written approval to engage in investment activities prohibited by this part but permitted by statute where the activities are part of a third-party investment program that NCUA has approved under this paragraph (c). A third party seeking approval of such a program must submit a request to the Director of the Office of Examination and Insurance that addresses the following items:

(1) A complete description of the activities, with specific examples of how a credit union will conduct them and how they will benefit a credit union.

(2) A description of any risks to a credit union from participating in the program.

**§ 703.150 What additional definitions apply to this part?**

The following definitions apply to this part:

*Adjusted trading* means selling an investment to a counterparty at a price above its current fair value and simultaneously purchasing or committing to purchase from the counterparty another investment at a price above its current fair value.

*Average life* means the weighted average time to principal repayment with the amount of the principal paydowns (both scheduled and unscheduled) as the weights.

*Bank note* means a direct, unconditional, and unsecured general obligation of a bank that ranks equally with all other senior unsecured indebtedness of the bank, except deposit liabilities and other obligations that are subject to any priorities or preferences.

*Banker's acceptance* means a time draft that is drawn on and accepted by a bank and that represents an irrevocable obligation of the bank.

*Commercial mortgage related security* means a mortgage related security where the mortgages are secured by real estate upon which is located a commercial structure.

*Deposit note* means an obligation of a bank that is similar to a certificate of deposit but is rated.

*Embedded option* means a characteristic of an investment that gives the issuer or holder the right to alter the level and timing of the cash flows of the investment. Embedded options include call and put provisions and interest rate caps and floors. Since a prepayment option in a mortgage is a type of call provision, a mortgage-backed security composed of mortgages that may be prepaid is an example of an investment with an embedded option.

*Eurodollar deposit* means a U.S. dollar-denominated deposit in a foreign branch of a United States depository institution.

*Fair value* means the price at which a security can be bought or sold in a current, arms length transaction between willing parties, other than in a forced or liquidation sale.

*Industry-recognized information provider* means an organization that obtains compensation by providing information to investors and receives no compensation for the purchase or sale of investments.

*Investment* means any security, obligation, account, deposit, or other item authorized for purchase by a federal credit union under Sections 107(7), 107(8), or 107(15) (B) or (C) of the Federal Credit Union Act, or this part, other than loans to members.

*Maturity* means the date the last principal amount of a security is scheduled to come due and does not mean the call date or the average life of the security.